

**City of Detroit**

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**OFFICE OF THE AUDITOR GENERAL**



**Audit of the Civic Center Department**

**June 2005**



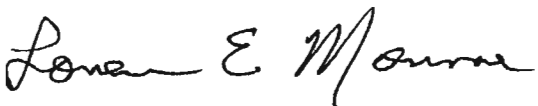
Loren E. Monroe, CPA  
Auditor General  
City of Detroit

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Detroit, Michigan 48226  
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## MEMORANDUM

**DATE:** March 14, 2006

**TO:** Honorable City Council

**FROM:** Loren E. Monroe  
Auditor General 

**RE:** Audit of the Civic Center Department

**C:** Mayor Kwame M. Kilpatrick  
Glenn Blanton, Director

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Attached for your review is our report on the audit of the Civic Center Department.

This report contains our audit purpose, scope, objectives, and methodology; background; status of prior findings; our audit findings and recommendations; and the agency's response.

We would like to thank the Civic Center Department's staff for the cooperation and assistance extended to us during this audit.

Copies of Office of the Auditor General reports can be found on our web site at [www.ci.detroit.mi.us/legislative/CharterAppointments/AuditorGeneral](http://www.ci.detroit.mi.us/legislative/CharterAppointments/AuditorGeneral).

## **Audit of the Civic Center Department**

**June 2005**

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#### **AGENCY'S RESPONSE**

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\* Finding appeared in the prior audit report dated March 2000.

## **AUDIT PURPOSE, SCOPE, OBJECTIVES, AND METHODOLOGY**

### **Audit Purpose**

The audit of the Civic Center Department (Civic Center) was performed in accordance with the Office of the Auditor General's (OAG) Charter mandate to audit financial transactions of all City agencies.

### **Audit Scope**

The OAG performed an assessment of the Civic Center's internal controls over cash receipts, payroll, voucher disbursements, fixed assets, inventory, and imprest cash transactions and determined that there are certain weaknesses in the system of control. We focused our audit on the weaknesses discovered during the assessment, and on the status of the prior audit findings.

Our audit was conducted in accordance with Government Auditing Standards issued by the Comptroller General of the United States, except for the completion of an external peer review within the last three years.

### **Audit Objectives**

Our audit objectives were:

- To evaluate the adequacy of the Civic Center's internal controls over financial transactions, and
- To determine whether the Civic Center implemented the prior audit recommendations or otherwise resolved the findings.

### **Audit Methodology**

To accomplish the audit objectives, our audit work included:

- A review of City ordinances, rental permits, and other pertinent information related to the Civic Center;
- A review of City directives, policies and procedures;
- Interviews with Civic Center management and personnel to gain an understanding of the agency's internal control structure;
- An evaluation of the Civic Center's internal controls over its major financial systems; and
- An examination of a sample of transactions that we considered satisfactory to achieve our objectives.

## BACKGROUND

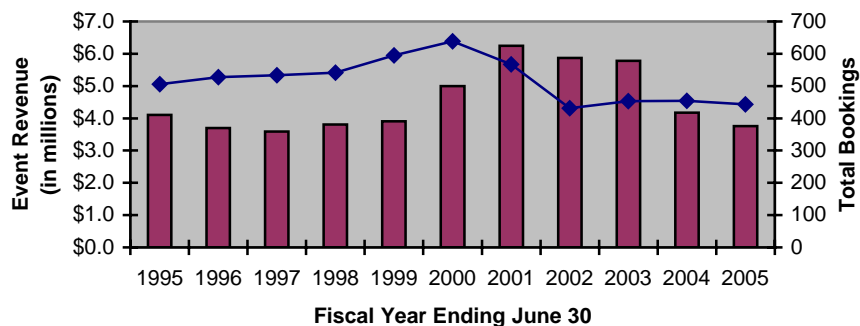
The Civic Center Department's purpose is to provide and promote world-class facilities and services for conventions, trade shows, banquets, special events, cultural events, major public events, and sporting events in order to create both a temporary and a permanent positive economic impact on the City of Detroit (City). The Civic Center Department is responsible for operational, marketing, and contract oversight for the Veteran's Memorial Building, Henry and Edsel Ford Auditorium, Cobo Center, Cobo Arena, Joe Louis Arena, and Hart Plaza.

The director of the Civic Center Department is appointed by the Mayor, as is a seven-member commission that serves in an advisory capacity to the director. Commission members receive no compensation.

One of the Civic Center's goals is to "Increase bookings and event-generated revenue through proactive initiatives, causing an increased demand for hospitality services that relate to Cobo activity." Our previous report concluded that for fiscal years 1996-1997 to 1998-1999 the Civic Center, in a competitive environment, satisfactorily met its performance goals to increase its event bookings and revenue by 3% to 5% over the previous year.

Event bookings and revenue for fiscal years 1994-1995 to 2004-2005 are shown in the chart below. Events include conventions and trade shows, public shows, conferences, banquets, and other rentals, including rentals to City agencies. Cobo has averaged 517 events annually, including those sponsored by City agencies, over the past 11 fiscal years. Over the past six years, Cobo has averaged 341 events sponsored by non-City agencies annually. Event revenue is comprised of building rentals, miscellaneous concessions, restaurant concessions, checking concessions, and equipment rentals.

**Event Revenue and Booking Trends**



The number of bookings rose between fiscal years 1994-1995 and 1999-2000, then sharply declined in fiscal years 2000-2001 and 2001-2002, and has remained relatively stable between fiscal years 2001-2002 and 2004-2005. In total, the number of bookings declined 12% between fiscal years 1994-1995 and 2004-2005. The number of bookings sponsored by non-City agencies declined 13% between fiscal years 1999-2000 and 2004-2005, the years for which information was available.

Event revenue climbed between fiscal years 1994-1995 and 2000-2001, dropped slightly in fiscal years 2001-2002 and 2002-2003, and dramatically declined in fiscal years 2003-2004 and 2004-2005. \$1.5 million of the \$1.6 million decline in event revenue in fiscal year 2003-2004 is due to the decrease from 15% to 3% in the commission rate earned on the sales of electrical services to exhibitors. The commission rate reduction impacted fiscal year 2004-2005's event revenue as well; 65% of the additional decline in revenue is due to the deduction of 2004 North American International Auto Show (NAIAS) expenditures from 2005 NAIAS commission revenue. The net amount was posted as fiscal year 2004-2005 event revenue.

The following is a summary of the Civic Center's budgeted and actual revenues for fiscal years ended June 30, 2003, 2004, and 2005.

Fiscal Year Ended June 30 - (In Thousands)						
	2003		2004		2005	
	Budget	Actual	Budget	Actual	Budget	Actual
Operating Income	\$ 7,494	\$ 7,090	\$ 7,510	\$ 5,628	\$ 8,436	\$ 5,341
Operating Expenditures	<u>17,642</u>	<u>20,763</u>	<u>26,851</u>	<u>24,140</u>	<u>25,332</u>	<u>23,185</u>
Net Income (Loss) From Operations	(\$10,148)	(\$13,673)	(\$19,341)	(\$18,512)	(\$16,896)	(\$17,844)
Add:						
Other Revenues	\$11,057	\$ 9,564	\$ 2,959	\$ 22 (1)(2)	\$ 702	\$ 7 (2)
Other Financing Sources	78	78	79	79	79	79
Other Income	<u>\$11,135</u>	<u>\$ 9,642</u>	<u>\$ 3,038</u>	<u>\$ 101</u>	<u>\$ 781</u>	<u>\$ 86</u>
Less: Fixed Charges	<u>(2,402)</u>	<u>(2,404)</u>	<u>(2,418)</u>	<u>(2,391)</u>	<u>(2,421)</u>	<u>(2,381)</u>
Net Tax Cost	<u>(\$1,415)</u>	<u>(\$6,435)</u>	<u>(\$18,721)</u>	<u>(\$20,802)</u>	<u>(\$18,536)</u>	<u>(\$20,139)</u>

(1) In 2004, the Detroit Building Authority received approximately \$1,470,500 in insurance proceeds that had been budgeted for the Civic Center Department.

(2) In 2004, \$1,468,000 of Miscellaneous Receipts was budgeted for Hart Plaza activities; in 2005, \$700,000 was budgeted. In 2004 and 2005, the Recreation Department, rather than the Civic Center Department, received the revenue generated by Hart Plaza events.

## **STATUS OF PRIOR FINDINGS**

The Office of the Auditor General's (OAG) March 2000 audit of the Civic Center Department included three findings with corresponding recommendations. A fourth finding reported the Civic Center's efforts to meet its goal to increase the number of events and event revenue.

Two of the findings have been resolved:

- The Civic Center separated the duties of recording cash receipts for room rentals into the Detroit Resource Management System (DRMS) General Ledger Module from the handling of the cash receipts.
- The Civic Center performed independent audits of its imprest cash fund.

One finding has not been addressed:

- The Civic Center does not record detailed explanations for granting discounts on the rental prices of its facilities. This finding is repeated.

As noted in the background section, while the Civic Center's efforts to increase event bookings has been successful in some years, overall, event bookings have declined by 12% between fiscal years 1994-1995 and 2004-2005 and has declined by 13% in events booked by external parties between fiscal years 2000-2001 and 2004-2005. Event revenue increased from the fiscal year 1994-1995 level, with substantial increases between fiscal year 1999-2000 and 2002-2003. Event revenue declined in fiscal years 2003-2004 and 2004-2005 due to the reduction in the commission rate earned on electrical services provided to exhibitors and the netting of 2004 North American International Auto Show (NAIAS) expenditures against the 2005 NAIAS revenue.

## FINDINGS AND RECOMMENDATIONS

An asterisk (\*) indicates that the finding and recommendation appeared in the previous Office of the Auditor General report.

### **1. Terms of Exhibitor Electrical Services Contract Were Intentionally Disregarded**

The Civic Center purchased electrical services at higher rates and earned lower commission revenue than those specified in the exhibitor electrical services contract. The Civic Center's rates were established in the Civic Center's contract for a sole-source vendor to provide electrical services to exhibitors.

- Greyhound Electrical Services, Inc. (GES) billed the Civic Center at rates higher than specified in the contract in 2001, and at the rate charged to exhibitors in 2003. Metro Services Organization, Inc. (MSO) billed the Civic Center for electrical labor at the rate charged to exhibitors during 2004 and the first half of 2005. The Civic Center was unable to provide copies of invoices for the electrical services it received in 2002.
- The Civic Center accepted a reduced commission on labor and materials provided by MSO to exhibitors at Cobo Center in 2003, 2004, and 2005. The rate was reduced from 15% to 3% in February 2003 for several events. The Civic Center extended the commission rate reduction to all events utilizing MSO during 2004 and the first half of 2005.
- MSO did not remit commission payments for the six months between June and November 2004 until February 2005.

The department's former director authorized the change in commission rate, and approved the invoices for payment with the higher labor rates. The Civic Center did not seek a formal amendment to the contract and approval from City Council for these changes.

Section 18-5-5 of Detroit's Purchasing Ordinance requires that all revenue contracts and contract amendments be approved by the City Council. The Civic Center's contract for exhibitor electrical services (effective July 1, 1994, and extended to June 30, 2005) called for GES to: pay the Civic Center a commission on the sales of electrical services at a rate of 15% of revenue earned, remit commission proceeds before the 15<sup>th</sup> of the following month, and bill the Civic Center for services provided at the contractor's documented labor cost plus 5%. GES assigned its rights to the contract to MSO in February 2003. Section 27.2 of the contract between the Civic Center and GES specifies that in order for a contract amendment to be binding, it must be in writing, both parties must authorize it, and it must be approved by City Council.

A Civic Center representative stated that it was not uncommon for the former director to alter contract terms without formal approval. The Civic Center's reasons for accepting changes to the contract terms follow:

- The former director authorized invoices for payment at rates higher than those contracted, and the reduction in the commission rate. Subsequent to his leaving, the Civic Center continued to honor the reduced rates that had been approved by the former director.



- The Civic Center did not process a contract amendment for the commission rate reduction because it considered the reduction temporary and necessary due to increased competition from other venues. Several exhibitors moved their events to other venues due in part to the Civic Center's high electrical rates. In 2003, MSO did not increase its rate to exhibitors as planned, and the Civic Center reduced its commission rate from 15% to 3% to offset MSO's reduced profit margin.
- MSO made late revenue payments to the Civic Center because the Civic Center owed MSO for services rendered.

The reduction from 15% to 3% of the commission earned on exhibitor electrical services resulted in a loss of over \$1.5 million in Civic Center revenue in fiscal year 2003-2004 and of nearly \$1.3 million on the 2005 Auto Show alone. The Civic Center Director disregarded the safeguard that was built into the contract to prevent it from paying excessively high, non-competitive, rates for electrician labor. Paying the exhibitor rate for services received resulted in the Civic Center paying between 24% and 50% more for short-term journeyman and foreman labor and between 31% and 65% more for long-term journeyman and foreman labor than the contracted rate.

### **Recommendations**

We recommend that the Civic Center comply with the City's requirement that contracts and amendments be formally approved by the Budget and Finance Departments and by City Council.

We also recommend that the Civic Center contract for electrical services over the short-term so that it has more flexibility to provide competitively priced services to exhibitors.

Finally, we recommend that the Civic Center implement a process whereby invoices are verified for compliance with contract terms before they are approved for payment, and that revenues due the City are monitored so they are received timely. Instances of management override of controls should be reported to the Chief Financial Officer.

## **2. Electrical Services Were Obtained Without Regard to the City's Purchasing Requirements**

The Civic Center circumvented the City's purchasing and accounts payable processes during fiscal years ended June 30 2001, 2002, 2003, 2004 and 2005. Civic Center management allowed its electrical contractors to deduct at least \$962,286 in invoice amounts owed to the contractors from the electrical sales commission revenue due to the Civic Center rather than process the transactions through the City's purchasing and accounts payable systems. The Civic Center posted the net amount it received from the contractor as revenue, and did not recognize amounts spent on electrical services, repairs and maintenance as departmental expenditures.

The following table shows, for each fiscal year, the North American International Auto Show (NAIAS) electrical sales commissions that were earned and that should have been recognized as revenue, the amount of electrical services received that should have been recognized as expenditures, and the amount of electrical sales revenue that was actually recognized. In most years, revenue and expenditures from the same year were netted; however, \$273,532 of expenditures from the 2004 NAIAS and Society of Automotive Engineers convention was deducted from the electrical sales commission revenue for the 2005 Auto Show.

	<b>Fiscal Year 2000-2001</b>	<b>Fiscal Year 2001-2002</b>	<b>Fiscal Year 2002-2003</b>	<b>Fiscal Year 2003-2004</b>	<b>Fiscal Year 2004-2005</b>	<b>Total</b>
NAIAS Electrical Sales Commission Earned	\$1,373,624	\$1,474,445	\$1,808,171	\$339,814	\$323,699	\$5,319,753
Electrical Services Received	102,876	223,580	312,705	273,532	49,593	962,286
Expenditures Deducted	102,876	223,580	312,705	0	323,125	962,286
NAIAS Electrical Sales Revenue Recognized	\$1,270,748	\$1,250,865	\$1,495,466	\$339,814	\$ 574	\$4,357,467

The contract for exhibitor electrical services does not require the Civic Center Department to purchase its electrical services from the contractor, however it does contain provisions that allow the Civic Center to engage services from the contractor at a competitive price. The contract states that the invoices will be processed as an "expedited requisition" (an emergency purchase) and will be paid in accordance with standard City of Detroit purchasing procedures. Section 18-5-5 (b) (1) of the City's purchasing ordinance allows emergency procurement under certain circumstances provided that the purchase is made using the level of competition that is practical under the circumstances, that City Council is notified of the emergency procurement within one week of its occurrence, and that the contract is sent to City Council for approval within four weeks of the procurement.

The Civic Center circumvented the City's purchasing process because it was convenient to purchase electrical services from the contractor that was on site. Because purchase orders were not established in the purchasing system, it was necessary to deduct the invoices from the outstanding revenue amounts in order to pay them.

The Civic Center's circumvention of the purchasing process controls eliminated the required financial oversight of appropriations and revenues by the Budget and Finance Departments and City Council. Due to the lack of competition, there is no assurance that the Civic Center received electrical services at a competitive rate. The City's revenues, expenditures, and assets were understated because the net amounts were posted. Because of the erroneous financial entries, the Civic Center's financial results are misstated.

### **Recommendations**

We recommend that the Civic Center immediately adhere to all procurement guidelines that are stipulated in the City's purchasing ordinance and in the City's accounts payable process.

We further recommend that future contracts for services comply with the City's purchasing ordinance and not permit the Civic Center to purchase non-emergency services using the emergency purchases provision of the City's purchasing ordinance which bypasses the City's competitive bidding requirements.

### **3. Asset System Was Not Maintained**

As of June 30, 2005, the Civic Center had not entered 37 assets into the City's Capital Asset Management System (CAMS), in accordance with the City's capital asset policy and procedures. The 37 assets are as follows:

- Computer systems, laser printers, and other systems-related equipment identified during a physical inventory performed at fiscal year-end June 30, 2004. Equipment acquisition reports listing 34 assets lacked the cost and purchase date of the related equipment. The Civic Center said it could not find documentation containing the costs and dates of purchase.
- Two computer servers that were not affixed with the latest City of Detroit property tags and were not included on the Civic Center's asset listing.
- One photo printer that did not have a visible property identification tag.

The Civic Center did not submit the equipment acquisition reports and a Physical Inventory Verification form to the Finance Department Capital Asset Unit in accordance with the City's fiscal year 2004 year-end closing procedure and did not maintain records of the physical inventory it performed at fiscal year end 2003-2004.

The City's Capital Asset Policy Guide and Procedures manual states that:

- All capital assets (including real property, works of art, infrastructure, taggable, and controlled assets) shall be recorded in the City's Capital Management Asset System and reported to the Capital Asset Unit within three business days of receipt.
- The original acquisition forms must be forwarded to the Capital Asset Unit immediately after recording the assets in the Capital Asset System.
- City-owned taggable capital and controlled assets shall be affixed with the City of Detroit property tags within three business days of physical receipt of the assets by a City department.
- Computer workstations and laptops should be tagged and tracked even if their total cost is below \$1,000.
- Each department shall conduct an annual physical inventory of its capital assets. All inventory forms and inventory reports should be maintained for audit purposes.

The Civic Center's asset coordinator stated that he was not aware of the computer equipment prior to the June 30, 2004 physical inventory. It was his understanding that since the equipment had been acquired from the Information Technology Department (IT), it had been included in the CAMS under an IT location. Civic Center staff should have been aware of the purchased equipment because the City's financial system indicates that the Civic Center purchased computer-related assets in fiscal years 2002-2003, 2003-2004, and 2004-2005.

Failure to include the 37 assets in CAMS reduced the effectiveness of the Civic Center's controls over its assets. In addition, the CAMS is understated by the total cost of the 37 assets.

**Recommendation**

We recommend that the Civic Center comply with the City's fixed asset procedures, including maintaining a complete record of its assets in CAMS, submitting the appropriate asset maintenance forms to the Capital Asset Unit within the required timeframe, tagging assets, completing an annual physical inventory, retaining physical inventory forms, and complying with the City's year-end closing procedures.

#### **\*4. Reasons for Granting Discounts Were Not Documented**

The Civic Center Department does not document the reason for granting discounts on 12-month leases and on event rentals.

- The Civic Center granted a total of \$1,039,535 in discounts on 165 events between July 1, 2002 and June 30, 2005. A review of ten discounted events disclosed that the Civic Center provided a detailed explanation for the discount for only three of the events.
- The Civic Center leases space to seven companies that provide on-site set up services to exhibitors. In 2003, three of the rentals were discounted resulting in a reduction in lease revenue of \$15,069; in 2004, two of the leases were discounted resulting in a reduction in lease revenue of \$8,353. "Special per Director" was the reason documented for the reductions.

Tenant	Lease Period July 2003 – June 2004			Lease Period July 2004 – June 2005		
	Discounted			Discounted		
	Annual Rental Rate	Annual Rental Rate	Revenue Reduction	Annual Rental Rate	Annual Rental Rate	Revenue Reduction
Convention Show Services	\$ 6,728	\$ 12	\$ 6,716	\$ 6,728	no discount	\$ 0
Freeman Decorating	19,065	14,482	4,583	19,065	\$14,482	4,583
SBC	3,782	12	3,770	3,782	12	3,770
<b>Total Revenue Reduction</b>			<b>\$15,069</b>			<b>\$8,353</b>

It is management's responsibility to assure that its programs are managed with integrity. Controls to meet this responsibility, such as policies and procedures, should be in place and utilized to reasonably assure that resources are protected from waste, fraud, and mismanagement and that timely information is obtained, maintained, and reported for the purpose of decision making. Discounts represent a reduction in revenue to the Civic Center. Therefore, the Civic Center should fully disclose the reasons for granting discounts to provide assurance that the discounts granted are legitimate in fact and in appearance, and are granted consistently.

A representative from the Civic Center explained that the nature of its business is such that it is necessary to have the flexibility to grant discounts. The Civic Center director authorizes all discounts, which can be seasonal, competitive, or unique in nature. The representative stated that the notation "Per Director Discount" is the extent of its documentation. Another representative of the Civic Center stated that the tenants offering on-site set up services generate trade sales; therefore, it is worthwhile to the Civic Center to let them occupy a room for virtually no cost.

The current practice of recording "Per Director Discount" does not provide adequate information to determine whether discounts were warranted or were granted in a consistent manner. Without the added control of documenting the reason for granting discounts, the legitimacy of discounts could be questioned even when all discounts are properly granted.

**Recommendation**

We recommend that the Civic Center Department implement a practice of recording detailed reasons for extending discounts on all lease contracts and on event rental records.



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CIVIC CENTER DEPARTMENT  
Hart Plaza  
Cobo Arena  
Joe Louis Arena  
Veterans Memorial Bldg.

Kwame M. Kilpatrick  
MAYOR, CITY OF DETROIT

## ATTACHMENT A

February 17, 2006

Sharon L. Gipson, Interim Auditor General  
Office of the Auditor General  
2 Woodward Avenue, Room 208  
Detroit, Michigan 48226

Dear Ms. Gipson:

The following presents the Civic Center Department responses for the indicated findings and related recommendations in the June 2005 Audit of the Civic Center Department Report, as prepared by the Office of the Auditor General.

**Finding No. 1.** Terms of Exhibitor Electrical Services Contract Were Intentionally Disregarded

**Department's Response:**

***The Civic Center Department concurs with the Auditor General's recommendation, and we have formally advised our Electrical Contractor that "Effective Immediately" all terms and conditions of the Electrical Contract must be strictly adhered to.***

**Finding No. 2.** Electrical Services Were Obtained Without Regard to the City's Purchasing Requirements

**Department's Response:**

***The Civic Center Department is in complete agreement with the Auditor General's findings and all future purchases will be procured through the Purchasing Department and in adherence with the Purchasing Ordinance.***

**Finding No. 3.** Asset System Was Not Maintained

**Department's Response:**

***The Civic Center Department concurs with the Auditor General's findings and will adhere to the City of Detroit's Capital Asset Management System (CAMS) and have all qualifying assets inventoried and entered into CAMS.***



**Finding No. 4.** Reasons for Granting Discounts are not Documented

**Department's Response:**

***The Civic Center Department is in complete agreement with the Audit findings and will fully document all future discounts and make it a part of the client's permanent file.***

Sincerely,

Glenn Blanton  
Director